



compensation for this very important product. Constellation has reached the following conclusions that we would like to share:

- Generators should be compensated for the provision of reactive power.
- Reactive power compensation should be provided to all generators as a cost based capacity payment based upon the design of the generator and its capability to provide reactive power.
- The "AEP Methodology" is an acceptable mechanism to define the costs associated with providing reactive power; others should also be considered.
- Where real power production is impacted in order to provide reactive power, generators should be provided their lost opportunity costs. PJM implemented this approach after the 1999 low voltage event.
- Within design and safety limits, generators should be expected to follow instructions of the transmission provider with respect to provision of reactive power.
- Due to the local nature of reactive power, a market based system for reactive power compensation is not appropriate at this time. This topic deserves additional discussion, but under the best case, it appears to be a number of years down the road. It is also important to note that in 2003, Reactive Payments in PJM were only 0.52% of the total costs of serving load. The cost of implementing a market design change needs to be balanced against the benefits. Put another way, Constellation is a great fan of markets, but in some cases we recognize that other compensation mechanism may be more appropriate.
- As with any regulatory changes, existing arrangements need to be considered when changing the compensation mechanisms for generators.

Thanks for the opportunity to be here today and share our views on this important subject. I would be happy to answer any questions you may have.

Dated: March 8, 2005